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## GM-TOYOTA JOINT VENTURE NEGOTIATIONS

On May 25, 1983, General Motors Chairman and CEO Roger B. Smith gazed out of his office window on the 14th floor of GM World Headquarters in Detroit, Michigan. Almost 7000 miles away in Toyota City, Japan, Eiji Toyoda, Chairman of Toyota Motor Corporation, contemplated the scene on a *kakejiku* (hanging scroll) in a corner of his office. Over 3 months earlier, the two executives had signed a Memorandum of Understanding (MoU) to form a joint venture to assemble subcompact cars in the United States. But until outstanding issues were resolved, each party held the right to terminate negotiations without liability. As these two leaders of the largest US and Japanese industrial corporations stood in their respective headquarters, each considered the distance their companies needed to bridge before the joint venture they envisioned could become a reality.

The MoU, dated February 17, set forth the "basic parameters of this limited manufacturing arrangement." The proposed joint venture (JV) would assemble a car based on Toyota's Sprinter, a front-wheel drive subcompact, at GM's idle plant in Fremont, California (just outside San Francisco). This plant would have a nominal production capacity of 200,000 cars per year. The venture would sell these cars to GM for resale through GM dealers. GM and Toyota would equally split ownership of the JV and the seats on the board of directors. Toyota would designate the president. The companies had also agreed to base the price of the car on a market basket index and that Toyota would largely assume manufacturing responsibility. Other areas of agreement included quality assurance, technical assistance, financing, and the royalty and technical terms of the JV's license to manufacture Toyota's car (for more details, see Exhibit 1).

Remaining issues fell into three major categories. First, both GM and Toyota needed to agree that the JV showed prospects of adopting an "acceptable employee relations structure" within the next 120 days. Second, the proposed JV required the approval of both US and Japanese government agencies -- especially, the US Federal Trade Commission. Third, GM and Toyota needed to finalize issues related to the JV's legal and organizational structure, how GM and Toyota would supply the JV with components, how the JV would supply its car to GM, technical assistance, and product responsibility. GM and Toyota had agreed to commit their best efforts to complete this last set of agreements by May 15, 10 days ago. Toyota and the United Auto Workers (UAW) were just now holding their first formal discussions. Only 3 weeks remained of the 120-day period.

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Would these negotiations end as a repeat of past unsuccessful alliance proposals? Toyota had tried before to hook up with Ford; GM had tried with Honda.<sup>1</sup> How would GM and Toyota resolve the remaining issues? Would the chief executives and their negotiators meet the deadlines?

## I. THE TWO CORPORATIONS: HISTORICAL PROFILES

GM and Toyota made their reputations on domestic muscle. Each had long dominated its home market in the face of reputedly more internationally oriented arch-rivals, Ford and Nissan. Nevertheless, in 1983, GM and Toyota's production capabilities made them the first and third largest auto makers in the world.

### General Motors Corporation

In 1982 GM, a fully vertically-integrated producer of cars, trucks and related components, had \$60 billion in net sales and employed 657,000 people worldwide. As of mid-1983<sup>2</sup>, the company owned 120 facilities in 90 US cities in 26 states, including 25 plants exclusively devoted to automobile final assembly. GM also manufactured in over 37 other countries, including Australia (GM-Holden), Austria, Brazil, Canada, Federal Republic of Germany (Opel), France, Mexico, Spain, and the United Kingdom (Vauxhall and Bedford).

In 1982, GM produced almost 5 million cars worldwide. Of that number, 65% were made in the US, and 71.1% were sold in the US. In that market, GM held a 44.1% share.

Origins. The General Motors Corporation was formed in 1908 by William C. Durant to take over the assets of the failing Buick Motor Company, Oldsmobile, and a year later, the Oakland (now Pontiac) and Cadillac companies. From the beginning, the company committed itself to producing a range of cars to suit a variety of tastes and purchasing powers: "a car for every purse and purpose." It also set out to diversify broadly in automotive engineering and to integrate backward into component manufacture.

GM operated essentially as a holding company, largely influenced by bankers and the DuPont family, for the next 12 years. The company acquired Chevrolet (in 1918), two truck companies (organized in 1911 as GM Truck Co.), Guardian Frigerator (renamed Frigidaire Division), and Champion Ignition (renamed AC Spark Plug Co.), among numerous other companies.

The 1920 recession created a crisis that led to Durant's resignation and replacement by Alfred P. Sloan. The new president and CEO stayed at the helm until 1949, served as chairman of the board from 1937 until 1956, and remained a board member until his death at the age of 91

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in 1966. Early in his tenure, Sloan inaugurated the multidivisional organization structure that was still in place in 1983 (for details, see below “Organization and Leadership”).

After this consolidation, the company undertook its first significant expansion abroad. It established an assembly plant in Osaka, Japan in 1928 only to close it 11 years later on the eve of World War II. It also acquired Vauxhall Motors (UK) in 1925, 80% of Adam Opel (Germany) in 1929 and Holden's (Australia) in 1931. GM acquired the remainder of Opel in 1931. GM was not permitted to re-enter Japan after the war, and the company refrained from further expansion in autos for almost 30 years. Then in 1959, GM began manufacturing in Brazil. Soon after, the company opened a plant in Argentina.<sup>3</sup> In 1971, GM acquired 34.2% of Isuzu (Japan) and later increased this stake to 38-40%. In August, 1981, the company bought 5.3% of Suzuki (Japan).

Organization and Leadership. GM's core consisted of 5 auto divisions: Chevrolet, Pontiac, Buick, Oldsmobile and Cadillac (see Exhibit 2). Alfred Sloan had instituted strong central control over decisions with a financial impact on the corporation and rational, corporate product policy to reduce redundancy. Key principles of Sloan's philosophy, which remained largely in place in 1983, included: centralized policy-making, decentralized operating management, separation of product policy and budgeting powers, committee decision-making (individual sponsorship but not approval of programs), and systemization of major decisions. As one author wrote in 1979:

Strategic decision-making at GM, particularly as related to products, has always been an informal, team-oriented process, dependent more on the strength of the organization and its key players than on a formalized, written procedure. There is, however, a forward product planning group that provides a quarterly review of company strategic planning and long-range decisions.<sup>4</sup>

Two committees, in particular, were very powerful within corporate decision-making: the Executive Committee, and the Finance Committee. As GM's top policy-making group, the Executive Committee proposed and/or advocated projects. The Finance Committee separately reviewed all approved projects that required corporate capital allocations prior to submission to the Board of Directors. The Treasurer's Staff, based in New York City, assisted the Finance Committee.

Detroit-born and University of Michigan-educated, Roger Smith was appointed chairman and CEO on January 1, 1981. Smith, 58, rose through the financial side of GM. He joined the company as a general accounting clerk in 1949. Over time, he rose to the positions of treasurer, vice-president of Financial Staff, and from 1974 on, executive vice-president and member of both the finance and executive committees. His efforts were the driving force behind GM's adoption of sophisticated strategic planning. In early 1983, as GM celebrated its 75th anniversary, Smith entered the third year of his chairmanship.

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Recent Performance. In April, 1983, the *Wall Street Journal* bannered GM's financial results with the headline "GM Earnings Soared in the First Quarter On Jump in Production; Sales Rose 14%."<sup>5</sup> Net income for the quarter was \$653.1 million. The article attributed approximately \$409 million of that amount to gains from foreign currency exchange and sales of the company's finance and insurance units. The US car market had expanded by only 4% in sales above 1982 levels.

The 1983 figures represented a rebound from an earnings slide in which GM hit bottom in 1980. That year, the company suffered its first loss since 1921: -\$763 million on sales of \$58 billion. Net sales increased the next year, and net income moved back into the black (see Exhibit 3). In 1982, sales dropped to \$60 billion, but income nearly tripled to \$963 million. Still, earnings represented only 1.6% of sales. GM management stated in its 1982 annual report that this figure fell "far below the level of capital generation needed to operate the business successfully over the long term."

Automotive products accounted for 94.4% of GM's 1982 total corporate sales. Car production and sales had declined every year since 1978, from 5.4 million units sold in the US that year to 3.5 million in 1982. (For competitive performance and positions, see "US Auto Market" below.)

Small Car Challenge. GM was struggling to compete effectively in the small car market segment. Its principal subcompact entry, the Chevrolet Chevette, was selling poorly even at a loss of \$800 per vehicle. Adapted from overseas operations, and introduced to the US in 1976, it was already 7 years old. GM did not have product readily available to replace it.

## Toyota Motor Corporation

Toyota Motor Corporation (hereafter referred to as Toyota), a manufacturer of cars, trucks and buses with additional business in producing prefabricated housing and selling industrial vehicles, was headquartered in Toyota City, near Nagoya, about 330 kilometers west of Tokyo. The largest of the 56 companies constituting the family-run Toyota Group, Toyota achieved \$15 billion (¥3,849,544 million) in net sales in FY 1982 and employed 57,800 people. (The Toyota Group as a whole directly employed 145,130<sup>6</sup> and reportedly accounted for 3% of Japan's GNP.<sup>7</sup>) In addition to its massive complex of supplier and assembly plants in Toyota City, Toyota owned car knockdown (KD) set assembly operations in 17 countries (e.g., Australia, Malaysia, Pakistan, Philippines, South Africa, Thailand).

In 1982, Toyota produced 2.3 million cars worldwide, nearly all assembled in Japan. About 130,000 KD sets were shipped that year. The Japanese market absorbed about 52.1% of Toyota's output, for a domestic market share of 38.6%.<sup>8</sup>

Origins. Toyota Motor Company was established in 1937, when Kiichiro Toyoda split off the automotive department from Toyoda Automatic Loom Works (esta. 1926). The family

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adopted the name after a numerologist advised it that eight was its lucky number (Toyota required only 8 calligraphic strokes in Japanese writing, whereas Toyoda required 10). The new company set objectives to produce trucks more cheaply than did Ford Japan in Yokohama and GM in Osaka. Early on, many key components for the company's vehicles had to be sourced from the US.

World War II and the immediate post-war period brought a number of challenges for the company. Although it was removed from General Douglas MacArthur's list of giant business combines (*zaibatsu*) to be broken up, the occupation authorities forced the Toyota Group to spin off Nippondenso (an electronic components supplier) and Toyoda Spinning & Weaving as independent companies. In 1950, Toyota veered close to bankruptcy. The Bank of Japan and Mitsui Bank came to its aid but stipulated, among other conditions, that Toyota reconfigure its operations in order to make the sales department a separate company (Toyota Motor Sales). Exports of trucks to UN and US forces in Korea also aided Toyota's reconstruction.

Toyota produced its first car, the ToyotaSA (or "Toyopet") in 1947. But the company's first "true passenger car," in Eiji Toyoda's words<sup>9</sup>, was the Crown, introduced in 1955. Toyota established its first overseas assembly operation in 1962, in South Africa. Four years later, Toyota launched the Corolla, destined to become one of the most widely sold cars in the world.

Volkswagen's North American success with the Beetle motivated Toyota to export its first cars to the US in 1957: two Toyopet Crown sedans. Initially enthusiastic US customers found them too small, not very stylish, and poor highway performers. In 1961, Toyota sold only 576 cars in the US. Within the next few years, however, Toyota began exporting its Corona (introduced in Japan in 1960) and then the cheaper Corolla (introduced at home in 1968). In 1975, spurred by Corolla's hot performance (151,000 sold in the US out of 278,000 units sold worldwide), Toyota overtook VW as the leading importer in the US.<sup>10</sup> Yet the company's only production presence in the US as of May, 1983 was Toyota Long Beach Fabricators in California. Established in 1974, the company installed rear decks on imported Toyota truck chassis.

Organization and Leadership. The heart of the Toyota Group (see Exhibit 4a), Toyota Motor Corporation was headed by a board of directors that included the chairman and vice-chairman, president, 5 executive vice-presidents, auditors, and 40 directors across 3 levels (senior managing, managing, and common). Most directors held responsibility for particular departments although the "functional meeting" served as the essential decision-making unit (see Exhibit 4b).

The formally constituted functional meeting cut across department lines and controlled broad corporate functions. These functions included setting corporate goals (i.e., market share, return on investment, etc.) and managing production, cost control, quality assurance, safety, sanitation and environmental affairs. Each meeting consisted of a number of directors. Some meetings convened once a month, others, every other month.

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In the formal organizational hierarchy, the functional meetings reported to the "management meeting," an executive organization that consisted of all senior managing directors and the standing auditor. The management meeting held approval power over all functional meeting decisions. Unless the management meeting raised objections, the decisions of the functional meeting carried the force of corporation decisions. As one analyst observed: "*Nemawashi* (persuasion of individuals concerned with decisions in advance of formal meetings) is unnecessary at Toyota . . . . At Toyota, the functional meeting becomes the *nemawashi* negotiation."<sup>11</sup> Externally, Toyota earned the reputation of a conservative company that "would test even a stone bridge before they crossed."<sup>12</sup> Two dominant cultures coexisted in the company. Outsiders viewed the manufacturing arm, Toyota Motor Company in Toyota City, as a "country bumpkin"-- an image not unlike that of US midwest-based GM. Employees of the marketing arm, Tokyo-centric Toyota Motor Sales, took great pride in its cosmopolitan experience and international success. The two companies merged to form Toyota Motor Corporation on July 1, 1982. But after 30 years of separation, employees remained fiercely loyal to their respective "companies" as GM and Toyota began their talks.

Eiji Toyoda, who brought about the merger, was the nephew of the founder of the Toyota Group. Educated at the University of Tokyo in mechanical engineering, he joined Toyota Motor Company at its inception in 1937. He served as director, senior managing director, and executive vice-president before rising to the presidency in 1967. In 1950, he spent a month visiting US auto plants, to draw lessons from their operations about how to "properly" produce cars. His philosophy inspired much of Toyota's emphasis on manufacturing efficiency. Toyoda assumed the chairmanship of Toyota Motor Corporation on July 1, 1982.

Recent Performance. In late May, 1983, one month remained in Toyota's successful first fiscal year as Toyota Motor Corporation (July 1, 1982-June 30, 1983). Net sales exceeded the previous fiscal year's \$15 billion pace. Net income showed similar performance (see Exhibit 5).

Over the 1978-82 time period, net sales rose every year; 1982 sales represented a 47% increase over the 1978 figure. But other measures were less rosy. Factory sales (in units) and net income had already hit highs in 1980. Worldwide car production remained close to the 1980 level, at around 2.35 million units. The company sold 50,000 fewer cars in the US in 1982 than in 1980 although it maintained its 6.7% market share.

Political and Competitive Challenges. In winter 1979-80, Japanese automakers' gains in the US market began to provoke political reactions among US automakers, other industrialists, labor leaders, and politicians. Their lobbying efforts prompted intergovernmental negotiations to limit Japanese exports to the US and instigated several proposals of bills in the US Congress (see discussion below on "US Auto Market"). In 1983, debate continued in the US and Japan on these international and domestic political issues. Many parties expected Toyota to respond. Honda Motor Company, Toyota's main Japanese competitor in the US, had been assembling cars at its Marysville, Ohio plant since late 1982.

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Prior Negotiations with Ford. After much hesitation and a year of feasibility studies concerning production in the US, Toyota made an initial response to these pressures. In May, 1980, Eiji Toyoda proposed that the Ford Motor Company and Toyota form a joint venture to assemble a Toyota-designed small car in a Ford plant in the US. Over the following 15 months, the talks struck a number of hurdles. But the companies made progress on an agreement to assemble vans.

The talks completely broke down in mid-July, 1981. Spokesmen for the companies publicly attributed the breakdown to an inability to agree on a product. Other insiders faulted media coverage, discord within Toyota and Ford, and lack of direction in the talks. Outside observers also cited the parties' differing goals, Arab nations' threats to boycott Toyota (Ford did business in Israel), and the slump in the US auto market.

## II. THE US AUTO MARKET

Although the auto industry originated in Germany and France, the US quickly became the world's largest car market. The US share of total world car registrations reached as high as 80% and stood, in 1982, at 36.4%.<sup>13</sup> US retail sales (new registrations only) ranged from 8.3 to 11.3 million cars out of about 30 million sold worldwide each year from 1970 -1982.

### Players and Market Shares

After Henry Ford introduced the Model T (1908) and mass production (1913) at Ford, and Sloan reorganized GM, the two companies flourished. By the late 1920s, American auto companies made over 85% of the world's motor vehicles.<sup>14</sup> Home demand took off after World War II. The replacement segment of the market overtook the first time buyer segment as a percentage of purchases after 1950, yet the market as a whole continued to expand.

1980 marked a dramatic change: Many observers saw it as the worst year in the US automotive industry since the 1930s. After hitting 11.3 million units in 1978 and 10.6 million units in 1979, retail sales plummeted to 8.97 million. The market continued to contract, falling to 7.98 million in 1982 (see Exhibit 6a and compare it to Exhibit 6b).

In mid-1983, the Big Three (GM, Ford, Chrysler) and American Motors (AMC) together held 71% of their home market. Their respective shares were: GM, 44.1%; Ford, 16.9%; Chrysler, 8.7%; and AMC, 1.4% (see Exhibit 6c). But these shares represented a declining trend. Only 4 years earlier, for example, GM held 47.5% of the US market. Each 1% decline cost \$350 million in sales.<sup>15</sup>

Only two other notable producers operated US facilities: Volkswagen of America (1982 production of 91,166 cars; 1.1% market share) and Checker (2000 cars). Several other

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companies, however, participated via imports. Their aggregate share had risen from less than .3% in 1950, to 6% in 1960 to 15.2% in 1970. Totaling almost 30% share by 1982 (that is, nearly one in every three cars sold), the shares of these importers were categorized as follows: Toyota, 6.7%; Datsun ("Nissan" in Japan), 5.9%; Honda, 4.6%; Toyo Kogyo (later named Mazda), 2.1%; Fuji (Subaru), 1.9%; VW imports, .8%; all others, less than 1.0% each.

### Shifting Demand for Small Cars

In the 1950s and 1960s, American consumers were interested in the styling and size of cars. By the mid-1960s, a pricing system largely based on car size had developed (see the classifications below). Performance also played an important role in many car buyers' purchase decisions.

Around 1972, however, American consumers began to show a significant interest in small cars. Two major events solidified the trend: the October, 1973 oil embargo and the Iranian Revolution in 1979. The first crisis caused gasoline prices to rise 20% in 1974. These prices and demand for small cars receded after the crisis passed. The second crisis left December, 1980 fuel prices 41% higher than the average 1979 price. The ensuing recession led consumers to delay car purchases and reinforced concern about "gas guzzlers" and fuel economy as a product feature. In 1975, the US Federal Energy Policy and Conservation Act also set a schedule of progressive, annual standards for corporate average fuel economy (CAFE) of automakers' product lines. The 1978 goal was set at 18 miles per US gallon (mpg).

The table below documents the preference shift to small cars. Purchases of domestically produced subcompact and compact cars increased 13.2% over the 1971-1980 period, and imports, which tended to fall into the same two categories, rose 11.5%.<sup>16</sup>

<u>Size</u>	<u>% Share of US Market</u>	
	<u>1971</u>	<u>1980</u>
<i>domestic</i>		
subcompact (wheel base <100")	7.42	15.41
compact (101-102")	15.79	20.96
intermediate (103-110")	20.84	21.37
standard size (>110")	37.07	11.09
luxury (defined by automaker)	3.66	4.48
<i>imports</i> (total)	15.22	26.69

In 1974, American automakers began "downsizing" their products by reducing their weight and spatial dimensions. In 1974, for example, GM's models averaged 4460 lbs. and 12 mpg; in 1981, the line averaged 3570 lbs. and 23 mpg.<sup>17</sup> US automakers had returned to producing large cars after the first oil crisis; they did not make the same mistake after the second one.



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## Japanese Imports

Despite their difficult entries into the US in the late 1950s, Toyota and other Japanese manufacturers' exports continued to penetrate the market. By the late 60s, Toyota owned a fleet of ocean transports that each carried about 1000 vehicles on its voyages to the US. In 1972, Japan overtook Germany as the No. 1 exporter of cars to the US. Toyota and Nissan spearheaded this turnaround, as one industry observer put it, through "a combination of industrial efficiency, intelligent marketing, good fortune, and the simple fact that they were able to offer Americans a superior product at low (even bargain) prices."<sup>18</sup> By the late 1970s, Japanese autos were acquiring a reputation for "fit and finish" as well as fuel economy.

In the winter of 1979-80, these gains contrasted with the bleak fortunes of the US Big Three. While their unit sales and revenues dropped (see earlier section on Players and Market Shares), Japanese import sales in the US continued to climb. From 1978-79, the top 5 Japanese importers' total sales (including Toyota, Datsun, Honda, Subaru, Toyo Kogyo) rose 31%, from 1.23 million to 1.62 million. These events repeated a scenario that had played out in other product markets, including textiles, steel, and color televisions. The context of this larger trade relationship, coupled with the auto industries' national salience, heightened tensions in both Japan and the US.

In Japan, the auto industry accounted for an estimated 11.5% of the 1983 total production value of major manufacturing industries. Out of a total labor force of about 50 million, 1 out of every 10 workers took part, either directly or indirectly, in auto-related work.<sup>19</sup> In 1983, 9 major automakers competed to serve a domestic market of only 2.5-3.0 million cars. Exports were critical to the industry's survival in its existing structure.

Auto exports accounted for nearly 45% of Japan's 1983 total world trade of US\$165 billion.<sup>20</sup> Among its customers for total exports, the US led with \$60.4 billion in purchases. About 45% of that figure derived from autos. The US also exported more goods to Japan than any other country (US\$26.9 billion). Nonetheless, beginning in the mid 1960s, Japan enjoyed a continuous net surplus in its merchandise trade with the US.

The US road transportation sector, including the motor vehicle industry, road construction and maintenance, as well as the transport of goods, services, and people, produced over 18% of gross national product in 1978. Motor vehicle industry and allied sectors' employment exceeded 14 million that year. The combined sectors accounted for about 20% of the total US job market-- 1 in every 5 private, non-agricultural jobs.<sup>21</sup> Then between 1978 and August, 1980, US automakers laid off 25% of the industry's labor force: over 250,000 workers. Chrysler alone permanently closed 10 plants. By 1983, 3,000 dealers had left the business. An additional 635,000 jobs in related industries were considered threatened. Meanwhile, the US trade deficit with Japan continued to grow.

These conditions and events led US labor leaders, politicians and industrialists to call for a variety of remedies that included domestic content legislation. From the Japanese, they

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demanded export limits and liberalization of the domestic market for autos and auto parts. UAW President Douglas Fraser announced in November, 1979 that the union would boycott Japanese cars unless Toyota and Nissan built assembly plants in the US. In February, 1980, US Steel Chairman David Roderick charged that Toyota and Nissan were dumping their cars in the US, at prices 14-20% below those in Japan. In December, 1981, a bill (HR5133) requiring 50% domestic content was introduced in the US House of Representatives.

Japanese leaders responded with concern. Some asserted that their imports created jobs in the US. The automobile import business directly employed over 150,000 people. In 1981, Toyota Motor Sales, USA employed 36,000 people and spent over \$1.7 billion on payroll, supplies and taxes. (In 1981, Toyota placed over \$189 million in orders with US suppliers, up from \$98 million in 1979.<sup>22</sup>) Labor leaders in Japan expressed concerns about job losses there. Toyota's union leader asserted that manufacturing 200,000 cars in the US (the capacity of an average assembly plant) would cost 40,000 Japanese jobs.<sup>23</sup> Eiji Toyoda, among others, raised concern about the ability of Japanese companies to effectively compete using US production facilities and labor. Still, during early 1980, the Ministry of International Trade and Industry (MITI) began pressing Nissan and Toyota to invest in the US.

Although Honda and Nissan promptly announced plans to invest in the US, interagency teams representing the two governments began negotiations over "voluntary restraints" on Japanese auto exports in April, 1980. Thirteen months later, in May, 1981, they reached an agreement, and MITI issued its first voluntary export restraint on autos. This plan covered a 2-year period. For the 1981-82 fiscal year (April 1-March 31), the Japanese government agreed to hold exports at 1.68 million units, which MITI described as a 7.7% reduction from the 1980 level. The agreement charged the Japan Automobile Manufacturers Association (JAMA) with the responsibility to monitor compliance. The automakers shared each year's quota according to their US market shares of the previous year. Shortly before GM and Toyota signed their MoU in February, 1983, MITI announced a third year of export restraints (April 1, 1983 to March 31, 1984) at the 1.68 million level.

### Japanese Direct Investment

In response to trade complaints, a number of Japanese companies made direct investments in the US in the 1970s. In 1972, Sony opened the first Japanese plant in the US, a television facility in San Diego. Other major investments included: Fujitsu's purchase of 30% of Amdahl (1971); Mitsui & Company and Nippon Steel's \$350 million purchase of 50% of Alumax, an aluminum maker (1973); Matsushita Electric's \$175 million acquisition of Quasar (1974); Mitsubishi International's \$300 million for one third of Kennecott's copper mining operation in New Mexico (March, 1983); and Fuji Bank's \$425 million for Heller International, a finance company (March, 1983).

Honda took the auto industry lead by announcing plans in January, 1980 to produce in the US. Nissan followed in April. In July, 1980, newspapers announced (prematurely, it turned out)

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that Toyota and Ford had agreed to form a joint venture to assemble cars. Honda began operations in November, 1982. By late May, 1983, only a few weeks remained before Nissan would start up its light truck assembly line .

The cumulation of Japanese investments in so many sectors of the US economy raised concerns in their own right. It would be a few months later, in early 1984, that the Director of Central Intelligence would denounce Japanese stakes in US computer companies as "Trojan horses" and caution Americans against overdependence on Japanese technology.<sup>24</sup>

### III. THE WORLD AUTO INDUSTRY

GM and Toyota made their plans to join forces not only in the context of a volatile bilateral market relationship between the US and Japan, but also in the context of a fast-changing worldwide industry. In 1980, the six major auto-producing countries consisted of the US and Canada (integrated under the US-Canada Auto Pact of 1965), Japan, the Federal Republic of Germany, France and the United Kingdom. Together, these countries produced 27,245,779 cars, or 75% of worldwide production of 36 million cars. The main producers included 4 companies in the US (GM, Ford, Chrysler, and AMC); 9 in Japan (Toyota, Nissan, Honda, Toyo Kogyo, Mitsubishi, Fuji, Isuzu, Suzuki, and Daihatsu); and 4 in Europe (Volkswagen, Fiat, Renault, and Citroen-Peugeot). The top 10 manufacturers in the world included two American, four Japanese and four European companies, accounting for 70.7% of world production.<sup>25</sup>

Automobile production required a variety of activities, from design to final assembly. These processes, combined, took 4-8 years. Investments in new models could run as high as US\$1.5-3.0 billion. Generally, manufacturing involved stamping, casting, engine and transmission machining and assembly, body welding, and final assembly (see Exhibit 7). A completed car comprised 15,000-20,000 parts, which represented 25-45% of the car's cost (see "Toyota Production System," below).

In the early 1980s, internationalization continued to bring about significant restructuring in the industry. In 1977, US companies manufactured 43.3% of the 24 million vehicle output of the six main producing countries. By 1981, however, they produced only 33.3% of 21.1 million vehicles. The European countries experienced smaller decreases: Their combined sales declined from 34.2% in 1977 to 33.6% in 1981. Japan gained substantial ground in this period, growing from 22.5% share in 1977 to 33.2% in 1981. In 1980, Japan overtook the US as the world's leading automobile manufacturer.

Most analysts offered similar explanations for the global shift in the auto industry. Japanese makers benefited from high levels of workmanship, lower wages, trade restrictions and protection of domestic industry, relatively weak structures of unionization, the advantages of a homogeneous society, the dollar-yen relationship (see Exhibit 10), and MITI's guidance. Meanwhile, observers argued, Americans committed managerial blunders, turned out inferior

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products, failed to respond to market forces, and suffered from worker dissatisfaction, low productivity (see Exhibit 8), and high wages. Less obvious explanations also presented themselves. Higher rates of inflation in the US forced prices for raw materials like steel, plastic, and copper to be higher than prices in Japan. During the 1970s, US federal and state regulations were significantly toughened in environmental, safety and other areas, creating the need for costly programs of compliance. The cooperative relationship between regulators and the regulated in Japan seemed to preclude such interventions.<sup>26</sup> These factors, combined with others, gave Japan a significant cost advantage. Even after shipping costs, Japanese automakers enjoyed a \$1,700 minimum cost advantage over US automakers in the \$5,000-\$6,000 retail price range (see Exhibit 8).

Significant changes also took place in the structure of import protection and in the number of vehicles moving in international trade. Between 1967 and 1978, average tariffs fell in all of the Triad economies: in the US, from 6.5% to 3%; in the European Community, from 22 to 11%; and in Japan, from 40% for small cars and 28% for others (1967) to 0% (1978). While Japanese exports to the US grew, Americans continued to sell at negligible levels in Japan.

#### IV. CURRENT CORPORATE STRATEGIES

##### GM's Strategy

GM had traditionally relied on its domestic market position as its main source of income. Before 1980, less than 25% of its total car sales occurred overseas. Ford, by comparison, sold over 48% of its production overseas. During the 1980s, GM's position in the US began to erode.

Part of the difficulty arose from GM's poor competitive position in the subcompact segment of the market. Production of a new small car to replace the Chevette was expected to take 5-7 years and involve a heavy investment. (GM had spent \$1.5 billion on the Chevette; Ford spent \$3.0 billion on its Escort. In both cases, the funds covered the costs of *adapting* the cars from overseas operations.) In Summer, 1981, GM canceled a proposed new small car after discovering that its partner Isuzu could build the same car for \$2000 less.

In mid-1979, *Business Week* reported that GM's long-range strategy was on track. It had used its "immense wealth" to jump 2 years ahead of its domestic competition in the 6-year shift to smaller cars. That year, after investing some \$2.5 billion, the company launched its fuel-efficient, front-wheel drive X-cars (e.g., the Chevy Citation). They sold well, due in part to the relative absence of direct competition.<sup>27</sup> But the X-cars had problems, as evidenced by four recalls in 1980 alone. By October, 1982, *Business Week* asserted that GM's strategy had "hit the skids."

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GM embarked on a new three-pronged strategy: 1) buy more parts abroad; 2) accelerate automation; and 3) pursue the "Asia strategy." In order to implement the first prong, GM scoured Europe and Asia for potential suppliers.

GM committed \$40 billion for the 1979-1986 period to implement the second prong, investing in new technology, plants, and cars. In 1982, GM joined forces with Japanese controls and robotics maker Fanuc to form GMFanuc. The joint venture set out to design and market factory automation robots from a Michigan base. In June, 1982, GM launched the Saturn project, "an all-out, all-American effort to beat the Japanese in the small-car market."<sup>28</sup> The company erected three brand-new plants -- the "last word in automation, sophisticated manufacturing systems, and enlightened labor relations" -- in Orion Township and Hamtramck, Michigan, and in Wentzville, Missouri. These plants, however, produced large, luxury cars.<sup>29</sup> Also in 1983, GM unveiled a blueprint for "the factory of the future," billed as "the ultimate in automation," in Saginaw, Michigan.

The third prong of GM's strategy involved selling captive imports under the GM nameplate. In 1981, GM contracted to buy "as many as 280,000" mini and subcompact cars per year from the two Japanese automakers in which it held equity: Isuzu and Suzuki.<sup>30</sup> (Consequently, GM opposed the restraints on Japanese exports that Ford and Chrysler supported.) With this strategy the company intended to delay the Japanese entry into the US market for as long as possible, learn as quickly as possible about Japanese manufacturing management methods, and minimize the time and costs involved in bringing its own new small car to the market.

Consistent with this strategy, GM began negotiations with Toyota in 1981, pursuing a number of specific interests. These included access to a new subcompact at a fraction of the investment required for in-house development, access to Japanese production technology, learning how to apply Japanese management methods in the US, and time to catch up with Toyota and match its per-vehicle cost advantage. As Chevrolet Vice-President Robert Stempel said in February, 1982: "In the amount of time it takes us to build one Chevette, they can build two Toyotas. The Fremont experiment is to see if we can do as well as the Japanese with American workers, American holidays, and American benefits." Another executive pointed out that the Chevette sold at \$5995, whereas Suzuki, which had contracted to supply GM, could deliver a mini-compact to the US for \$2900.<sup>31</sup>

## Toyota's Strategy

Like GM, Toyota had traditionally relied on its share of its domestic auto market as the principal source of its income and profit. Based on new registrations, Toyota's 1982 share of 38.6% represented a slight increase over its 1978 share of 37.9%.<sup>32</sup> More dramatically, by 1981, Toyota's overseas sales hovered around 50% of its worldwide car sales.

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Racing for dominance over Nissan in the US import market, Toyota had exploited its ability to learn from its mistakes. Indeed, one of the pillars of its strategy was continuous improvement, or *kaizen* (see "Toyota Production System," below). By the 1980s, Toyota had set a goal of achieving "Global 10" (a 10% share of the world car market).

Much of Toyota's manufacturing strength stemmed from its massive supplier and production complex, Toyota City, in Japan's Aichi Prefecture, 64 kilometers from the wharves of Nagoya (discussed in detail under "Toyota Production System.") By May, 1983, the company operated 10 plants in this area, 4 of them just for final assembly of cars. With these logistical advantages, its wealth and conservative financial posture (which inspired the company nickname, "The Bank"), and its provincial roots, Toyota's management would have preferred to continue producing and shipping from this site. But protectionist pressures from the US and Europe pushed the company abroad.

Toyota had limited international experience and significantly lagged behind Nissan in overseas manufacturing. Although the company operated 21 foreign plants in 1983, mostly in Asia, their operations were restricted to assembly of KD sets. Toyota had approached Ford about joint venture prospects on four occasions: in 1939, 1950, 1960 and finally, 1980. None of these initiatives succeeded.

Toyota Motor Corp. President Shojiro Toyoda commented on the GM negotiations, "We admit that we had difficulty with Ford, but we don't think that it will be the same . . . with GM. GM is now thinking about building smaller cars, but it is not confident enough to build those cars by itself in their idle plants. So for them it is better to shake hands with Toyota. As for Toyota, we are not confident about setting up a new plant and making it profitable. So both companies have their reasons."<sup>33</sup> In addition to financial risk and concerns about labor productivity, Toyota was concerned about its ability to manage a US plant and supplier network in its accustomed ways. Exposure to GM and its network, however, could teach Toyota much. Furthermore, Toyota clearly wanted to maintain access to the largest car market in the world.

## V. NEGOTIATIONS TO DATE

The idea of a joint venture between the two automotive giants arose as an informal initiative during the fall of 1981. On December 21, Toyota Motor Sales Chairman of the Board, Seisi Kato, called on Roger Smith in Detroit for what Smith later described as a "bewildering visit" (due to language barriers).<sup>34</sup>

Two months later on March 1, after considerable groundwork by GM, Roger Smith met Eiji Toyoda at the Links Club in New York City. Some news articles reported that Smith put forward a plan; others reported that Toyoda offered the initial proposal. But the basic concept resembled the Ford proposal: formation of a joint venture to assemble a Toyota-designed small car in a GM-owned plant in the US. GM President James F. McDonald said later that day that if

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the companies reached an agreement, the venture would annually assemble 400,000-500,000 cars.<sup>35</sup>

Some observers responded to the news with skepticism. Toyota's concerns about prospects for efficient US production were well-known. Its test factory in Long Beach, California lagged behind a similar factory in Japan by a factor of 30 percent. Furthermore, the meeting announcement preceded US-Japan trade talks by two days. Reportedly, Toyota had made "politically opportune" moves on other occasions.<sup>36</sup> Nonetheless, by the end of March, Smith and Toyota reached an agreement in principle to form a joint venture.

The first operational level negotiations opened in Tokyo on April 14, 1982. Jack Smith, Worldwide Product Planning Director, led the GM team, which also included Jay Chai, Executive Vice-President of C. Itoh & Company (America) and Advisor to the GM Chairman on Japanese Affairs; Louis Hughes, Assistant Treasurer, GM Financial Staff; Flavio Cella, a financial analyst; and one additional analyst. The seven Toyota representatives included a top executive, Toshio Morita, Executive Vice-President, Production Technology; T. Toyozumi, Director, Finance; T. Tsukada, Director, Legal Affairs; Kan Higashi, Director and General Manager, Overseas Projects; and three others. The second round of operational level negotiations took place from May 17-20. Chai, an American fluent in Japanese, facilitated these talks and others before and after them.

In June, Morita led a Toyota delegation to the US to survey a number of GM plants. According to Roger Smith, the negotiations then focused on sites in Georgia and Louisiana. But two California assembly plants dominated these possibilities and all others: one in South Gate (near Los Angeles) and the other in Fremont (near Oakland). In July, Smith reported that Toyota had started engineering and manufacturing studies for a potential joint venture.<sup>37</sup> By the end of the summer, the two companies reached agreement on such basic issues as the type of car, number to be produced, plant location (Fremont), and sales channels (see chronology, Exhibit 9).

The parties had expected full agreement by September, 1982. But on September 20, when Jack Smith brought his negotiating team to Tokyo for another round of talks, difficult issues remained. These included the valuation of the Fremont plant that GM would contribute, management of the operation, the licensing fee to Toyota, and the retail price of cars produced. Insiders told reporters that the companies might be trying to get too much from each other.<sup>38</sup> General Motors had invested \$280 million in Fremont, over half the cost of a new plant, less than one year before shutting it down in March, 1982. Toyota, with its concerns about a profitable and efficient operation, pushed for a high licensing fee and freedom to run the plant.<sup>39</sup> Other issues and obstacles included the effects of fluctuating exchange rates on complicated financial aspects of the agreement, the liability for warranty work and any legal disputes that might arise, and procurement/production arrangements for the 15,000 to 20,000 parts necessary to build the car.

Potential antitrust issues also remained. GM had anticipated this concern and consulted dozens of prominent antitrust experts including former high officials of the US Federal Trade

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Commission (FTC) and the Justice Department. Toyota also hired a prominent Washington law firm to advise it concerning the FTC. An outside attorney sat in on sessions to ensure that the negotiations did not stray into violation of US antitrust laws.

As talks unfolded through the fall, the parties revised their projections for an agreement to December. On his return from the US on November 29, Eiji Toyoda stated that the companies would not reach an agreement by the end of the year. Shortly thereafter, Roger Smith wrote to Toyoda softening GM's stand on plant valuation and urged him to agree. They promptly reached an agreement on valuation and on advance royalties that Toyota had requested from GM.

On December 23, Toyota Vice-Chairman Shigenobu Yamamoto and Managing Director Masami Iwasaki visited Roger Smith in Detroit and worked through some remaining issues concerning labor. One month later, on January 20, 1983, Jack Smith returned to Japan with the GM negotiating team. Throughout the year, the two companies' teams had focused their discussions on successive drafts of an MoU. During this round, the two companies worked on the 9th or 10th MoU draft.

On January 24, Soichiro Toyoda, said, "It is too early to predict the possibility of reaching a final agreement between our companies by the end of January."<sup>40</sup> Indeed, after another day of negotiations that produced no additional movement, GM negotiators feared that the deal would collapse. At a critical meeting on January 26, Jack Smith, Toyozumi and Chai revived it. They also resolved legal and termination issues that were reopened that evening. The teams drafted the final MoU on January 31.

The GM Board of Directors approved the agreement (for a second time) on February 7, giving Roger Smith authority to sign. GM then awaited news from Toyota. Toyota's Board met on February 14. Later that day -- Valentine's Day -- the two companies simultaneously issued press releases in the US and Japan announcing the agreement.

Roger Smith and Eiji Toyoda signed the MoU on February 17, 1983, in Fremont, California. It contained the following points:

- establishment of a new company equally owned by General Motors and by Toyota
    - \* Each principal would appoint an equal number of board members
    - \* Toyota would designate a president
  - the venture would produce a front-engine/front-wheel drive car derived from Toyota's Sprinter to sell directly to GM
  - the parent companies would provide equal shares of capital  
(Although the written agreement did not stipulate amounts, the parties had agreed to \$200 million in equity capital: \$100 million cash from Toyota, and \$11 million cash plus the Fremont plant (\$89 million) from GM. Another \$250 million were to be raised later.)
  - Toyota would design the Fremont manufacturing layout
  - a stamping plant would be constructed adjacent to the existing Fremont assembly plant
  - Toyota would receive a "reasonable royalty" for the license to manufacture the car
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- Toyota would be reimbursed for technical assistance on a cost-plus basis
  - the plant would have a nominal annual production capacity of 200,000 cars
  - the venture would price its cars on a market-basket standard (the weighted average of wholesale prices for 10 specified cars, see Exhibit 1A)
  - the venture would start up for the 1985 model year, beginning September, 1984
  - the agreement was contingent on the creation of an "acceptable employee relations structure" within 120 days.

Immediately after the signing, the two companies filed a request for approval of the joint venture with the FTC. One Washington-based attorney reportedly considered the five commissioners' decision difficult to predict. He noted, "They are very independent-minded."<sup>41</sup> Chrysler publicly criticized the proposed venture and pushed hard for a rejection. On April 18, its officials submitted a brief to the FTC and called for hearings. On the 28th, Chrysler announced that it would distribute a 38-page memo on why the joint venture would violate antitrust regulations. The company mounted what a Toyota attorney later called a "full-court press."

In May, 1983, GM and Toyota faced deadlines for agreements on labor relations, parts sourcing, and a number of other issues. In order to make the plant ready for operations on schedule, the partners needed to promptly issue bid requests for construction of the stamping plant. In short, major issues remained for resolution, and time was running out.

## VI. THE TOYOTA PRODUCTION SYSTEM

The Japanese automakers' success in the 1970s, particularly in achieving lower production costs, created considerable interest in their production methods. Many considered Toyota's system the best in Japan. American managers and workers wondered, however, if Toyota could effectively implement its methods in the US. Toyota officials wondered too.

### Key Concepts and Practices

Toyota's system was conceived by founder Kiichiro Toyoda and refined after World War II by Eiji Toyoda and Taiichi Ohno (an executive vice-president). Cost reduction was its essence. In addition to this primary goal, three subgoals included: 1) quantity control, which enabled the system to adapt both quantity and variety of products to demand fluctuations; 2) quality assurance; and 3) respect for humanity.<sup>42</sup> In practice, this philosophy resulted in a flow-type production system that built what was needed as needed.

Analysts of Japanese production systems use four terms to convey their essentials: just-in-time inventory (*kanban*), automation (*jidoka*), flexible work force (*shojinka*), and creative

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thinking (*soikufu*). Other concepts and terms that appeared in writings included continuous improvement (*kaizen*), elimination of waste (*muda*), and teamwork.

Just-in-time (JIT) inventory entails holding, near the assembly line, only the materials and parts needed to meet immediate needs. This could mean, for example, that a parts maker like Nippondenso, which supplied Toyota's Kamiggo engine plant with alternators, made as many as 21 deliveries a day<sup>43</sup> (see below "Relationships with Suppliers"). In US plants, in contrast, managers generally maintained 21 days' inventory. Operating without a buffer inventory required critical coordination between preceding and subsequent production processes, and between assemblers and suppliers. The system achieved part of this coordination by using *kanban*, cards of various colors, to give notice of parts needed for particular points-of-use in production processes.

Autonomation refers to work force-wide responsibility for defect control. It was designed to ensure that no process ever feeds a defective part into a succeeding process. Each and every line worker holds both the responsibility and authority to stop the assembly line if he or she detects a fault.

Toyota maintained a flexible work force by training workers for multiple functions, to permit them to move from one task to another, as shifts in demand changed production needs. This approach was also intended to stimulate workers' abilities. The Toyota culture demanded that every member work toward improvement through creative thinking and "inventive" ideas.

The final element, which an outside observer called "the cornerstone of the Toyota production system," consisted of production smoothing.<sup>44</sup> In order to adapt to changes in demand and minimize production process fluctuation, Toyota assembled finished cars in mixed batches reflecting the lowest multiples of a day's total factory order, rather than in long runs of single models. If a day's production requisition called for 500 Coronas including 400 sedans and 100 hatchbacks, for example, the line produced them in the sequence: sedan, sedan, sedan, sedan, hatchback, sedan, sedan, sedan, sedan, hatchback.

These features of the Toyota system offered several advantages. The JIT system eliminated the need for warehouses and reduced capital outflow. Indeed, under ideal circumstances, Toyota would sell finished products even before payments for materials and parts were due.<sup>45</sup> An American plant manager who studied Japanese systems estimated that JIT saved as much as \$500 per car. Reduced inventory requirements cut down plant clutter as well as overall size. The JIT system also kept suppliers in constant communication with Toyota and created incentives for pre-delivery quality assurance: Toyota speedily detected any defective parts and expected suppliers to immediately respond. This system also increased flexibility and quickened setup time. From 1945-1954, changing and setting up dies to change models took Toyota 2-3 hours. After 1970, the time dropped to 3 minutes.<sup>46</sup>

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## Relationships with Suppliers

As the heart of the Toyota Group, Toyota Motor Corporation relied on a vast network of affiliated companies for fully assembled cars as well as components. All told, 15,000-20,000 parts (alternatively, some 2000 subassemblies) made up a fully assembled car. Toyota held equity stakes in two assemblers, Daihatsu Motor Company (14.1%) and Hino Motors (10.3%). About 175 primary suppliers provided components. Of these, 56 were affiliated by ownership to the Toyota Group. Toyota itself produced engines, body panels, transmissions and instrument panels.

The two assemblers occupied similar roles in the Toyota Group. Toyota marketed Daihatsu's cars through its many overseas distributors and also subcontracted assembly operations for the smaller company in some of its KD plants around the world. Daihatsu subcontracted as an assembler of Toyota subcompacts and light trucks in Japan. Hino enjoyed similar, but more comprehensive ties to Toyota, linked by product planning, procurement, parts specification and cost reduction programs (see Exhibit 4a).

Toyota's component suppliers formed a tiered network.<sup>47</sup> In addition to the primary suppliers, 4,000 secondary and tertiary subcontractors and suppliers served the company. The primary 175 formed the membership of the Toyota Supplier Association, *Kyoho-kai* ("club for co-prospering with Toyota"). This organization, with three regional branches, helped Toyota to coordinate common policies among the suppliers and to set a uniform framework for annual purchasing contract negotiations.<sup>48</sup> (For names of particular suppliers, see Exhibit 4a).

Critics of this system suggested that Toyota and other companies nurtured their suppliers while simultaneously exerting extraordinary pressure on them to cut prices when market conditions worsened (notwithstanding the terms of existing contracts). Toyota had a reputation as a tough customer. Parts prices consistently declined, beginning in 1973. One Toyota-watcher commented, "It is the old feudal policy of 'don't let them live, but don't let them die.'" Toyota expected suppliers to open their books to Toyota auditors. Small, family-run businesses at the bottom of the supply pyramid grossed as little as \$1000 per month.<sup>49</sup>

Admirers of the system noted that "relational contracting"<sup>50</sup> enabled Japanese automakers to concentrate their purchases on relatively fewer suppliers than was the US practice and to work more closely with them in quality control and joint innovation engineering. The resulting long-term relationships and high levels of trust and loyalty may have improved suppliers' incentives to initiate innovations and improvements.

GM and Toyota negotiators considered the prospects for establishing Toyota's production system and supplier relationships in the US as a major issue. Negotiators needed to consider items, quantities, and order allocations between US and Japanese sources. Deliberations over parts delivered from Japan needed to anticipate fluctuations in the US\$/¥ exchange rate.

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## VII. US AUTO PARTS SUPPLIERS

The US auto supply network in the 1970s and 1980s exhibited significantly higher levels of OEM (Original Equipment Manufacturer) integration than did the Japanese industry. In 1980, nonetheless, over 40,000 independent suppliers participated. They were mainly concentrated in the midwest (see Exhibit 11). Over half employed fewer than 20 people.<sup>51</sup>

Major suppliers differentiated themselves by their reliability. Still, OEMs insisted that all suppliers maintain substantial inventories of both raw materials and finished goods, to reduce the risk of supply disruptions. Suppliers typically maintained 20% excess capacity for surge demand. The automakers also expected them to regard non-automotive customers as secondary priorities during peak demand periods. In addition, suppliers were expected to commit resources to pre-production engineering programs for new models.

OEMs generally maintained two or three subcontractors for any externally-sourced component. Policies precluded outsourcing complete systems from any one supplier. Items for which outsiders met partial needs were subject to regular "make-or-buy" reviews. Since internal sources could often document marginal savings, external suppliers frequently found themselves shut out of their standing contracts.

### The GM "Group"

GM typically sourced no more than 15% of its standard parts from independent suppliers. Purchased parts represented 50-53% of value-added for GM, compared to 66% for Chrysler.<sup>52</sup> Exhibit 13 lists the major parts of a car, and the four US automakers' relative levels of vertical integration. Even as the most highly-integrated US producer, GM purchased components and raw materials worth more than \$16 billion in 1974.<sup>53</sup>

GM's \$31 billion internal components business included 14 divisions with such names as Delco, Fisher Guide, Inland, Rochester Products, New Departure Hyatt, Packard Electric, AC Spark Plug, Harrison and others. The employees of these divisions outnumbered the combined work force of Ford and Chrysler.<sup>54</sup> Once a source of pride, cost control, reliable delivery and quality assurance, the internal divisions in the early 1980s began to fall behind the assembly and stamping plants that had drawn the focus of Roger Smith's modernization efforts. Despite frequent competitive outside bidding on parts contracts, it was difficult to discern the competitive positions of inside divisions vis-à-vis external suppliers on an arm's length basis.

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## VIII. LABOR-MANAGEMENT RELATIONSHIPS IN THE US

### UAW-Industry Relations: Background

The UAW, formally, the United Automobile, Aerospace and Agricultural Implement Workers of America, was established in 1935. Throughout the 1950s and 1960s, a fairly adversarial style characterized auto industry labor relations. The 113-day strike against GM in 1948 highlighted this quality for the era. More generally, from 1948-1962, the joint union/management grievance committee at GM settled an average 76,000 grievances per year.<sup>55</sup> During this period, wages increased each year.

From 1977 - 1983, Douglas Fraser led the union as president and became known, even among corporate executives, for the breadth of his outlook. On May 18, 1983, after elections at the union's triennial convention, Owen Beiber succeeded Douglas Fraser. Beiber had served in union positions for 22 years, most recently as vice-president and director of the GM Department. Some auto executives dubbed Beiber a "lunch pail" union leader: someone more concerned with grievances than with the overall structure of the industry.

On May 19th, Beiber held a press conference and announced the appointment of UAW Vice-President Donald Ephlin as director of the UAW's GM Department. Ephlin had spent 11 years as an officer of the local union attached to the GM Motor Assembly Plant in Framingham, Massachusetts before being appointed in 1960 to the International union staff as a member of the GM Department. During the 1970s, he served as the administrative assistant to UAW President Leonard Woodcock and participated in the negotiations with all of the Big Three. In addition, Ephlin and UAW Vice President Irving Bluestone were members of a joint GM-UAW committee whose primary focus was the quality of work life in GM plants. Elected vice president in 1980, Ephlin directed the union's Ford Department prior to his re-election as vice president in 1983 and appointment to the GM Department.

Union Rights to Organize and Collectively Bargain. Local chapters (or "locals") represented the work forces of particular plants. They could be organized and certified anywhere a majority of the work force voted in an open election for union representation. At the same time, right-to-work legislation such as that in California allowed employees not to join the union even if the union won a plant election. Regional and international representatives of the union generally conducted contract negotiations with the automakers.

Workers' rights to organize and collectively bargain with employers were secured under the Wagner Act, which Congress passed in 1935. The Act both provided rights to employees and prohibited any interference with these rights to: 1) be represented; 2) bargain collectively through representatives; 3) have their labor organization represent them without employer interference; 4) be protected against discrimination by employers for union activity; and 5) be protected against retaliation for accusations made regarding the illegal labor practices of employers. The Wagner Act also included the provisions that established the National Labor Relations Board (NLRB). Consisting of five members appointed by the US President and confirmed by the Senate, its

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primary duties included determining the legal applicability of claims filed by employees against employers and unions; and determining whether employees wanted union representation. The board did not initiate actions; it only responded to complaints filed by complainants. Boards with a majority of democrats tended to rule in favor of the unions, while republican-dominated boards favored employers.<sup>56</sup>

In practice, a union's authority to represent employees depended on showing that it had majority support from the workers in a given bargaining unit. If a company agreed that a union enjoyed majority support, no election needed to take place. The organization of a plant involved several steps. The first step required a "showing of interest," consisting of 30% of the employees in a relevant unit signing union cards, which authorized a union to act as a worker's representative. The union then submitted a demand for recognition to the employer, asserting that it had majority support. If the employer did not reject this assertion, it had to negotiate with the union. An employer could reject this assertion, however, based on a "good faith" doubt that the union enjoyed majority support. When an employer rejected a union's assertion of support, the union could petition the NLRB for an election. If the employer failed to execute an election agreement, the local NLRB could hold a hearing and issue a "Decision and Direction of Election." Once the election was held, and barring objections by either side, the NLRB would issue a "Certification of Results of the Election."<sup>57</sup>

Current Trends. In February, 1982, one year before GM and Toyota signed their MoU, a *Fortune* reporter wrote:

The UAW achieved wage rates that were among the highest in American industry for semiskilled labor, as well as an elaborate panoply of fringe benefits -- full pensions at any age after 30 years' service, company-paid unemployment benefits to supplement those paid by the government, 29 holidays in 1981 for workers at GM and Ford in addition to vacation time, sick pay insurance, and an extensive range of hospital, medical, dental and eye-care services. The average GM blue-collar employee received \$35,919 in wages and benefits in 1980 [\$21.50/hour, which included wages and benefits].

For two years it [the UAW] was engaged in . . . [cutting labor costs] . . . with Chrysler, trying to keep the company afloat...But all through 1981, the UAW had resisted the entreaties of Ford and GM to reopen their 3-year contracts. . . [due to expire Sept. 14 '82].

Then came an appalling third quarter . . . In January, the job hemorrhage was horrendous: out of 1.5 million members, 214,500 auto company employees were on indefinite layoff and 123,000 were temporarily jobless -- the latter being the highest number since the UAW has been collecting figures.<sup>58</sup>

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Indeed, the early 1980s seemed to herald changing times for the UAW and its members. In addition to granting wage concessions to Chrysler, UAW President Fraser took the unprecedented step of accepting a seat on the Chrysler board. But every year the union lost more and more of the asset on which its strength depended: membership. Dues-paying membership declined 10.5% each year from 1979 to 1983.<sup>59</sup> New, non-unionized American plants owned by Honda and planned by Nissan set examples that deeply concerned union officials. Workers at these plants, some former union members themselves, made such statements as "I seriously hope we never get the UAW in this place. They can't give me a thing Honda isn't giving me. I don't think the UAW can do any good here."<sup>60</sup>

At the same time, many rank-and-file union members did not "buy into" labor-management collaboration such as the "Quality of Work Life" programs begun in 1973, participatory decision-making, and self-managed work teams. Many took a dim view of changes in bargaining styles and relationships among top union and company officials. Many American autoworkers considered management "arrogant," and held it accountable for the companies' woes. Auto workers believed that management exaggerated the difficulties. As Fraser put it, they viewed the companies as "rich, even when they're not rich."<sup>61</sup>

## Apparent Contrasts with Japanese Labor-Management Practices

Japanese companies like Honda brought more than capital to the United States. Along with their investments, they brought a Japanese style of labor relations forged in adversity as Japan's automobile workers and companies pulled together to recover from the devastation of World War II. An initial period of labor-management confrontation in the early 1950s had given way to increased unemployment. Norms of collaboration emerged, based on unions' willingness to cooperate in efforts to improve productivity in exchange for an understanding that no workers would lose their jobs as a result. Unlike the UAW and other US unions, the Japanese organized unions on a company-by-company basis.

Many Japanese office and shop floor practices contrasted with those of Americans. At Honda's US plant, for example, management and workers reported to work in identical white cotton shirts and trousers and ate in the same cafeteria. More generally, cohorts of workers started together at the bottom level in Japanese companies, shared in daily meetings, and participated in production line decisions. Management solicited their suggestions. Other practices included morning group calisthenics, group rendition of the company song, and flexible task deployment.

American assessments of these practices varied. Some observers found Japanese companies "more people conscious than the West."<sup>62</sup> Others focused on practices such as relatively fast assembly line speeds and asserted that the collaborative atmosphere of labor-management relations in Japan depended on coercion. Also, UAW workers, accustomed to specialized jobs allocated by seniority and strict job classifications, were suspicious of flexible tasking. This debate was gathering force in the US in May, 1983.

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## The 1982 GM-UAW Agreement

On March 21, 1982, GM and the UAW concluded a new national agreement to replace the contract scheduled to expire in September. Ratified by a majority of the UAW membership in early April, the contract took effect April 12, 1982, to run to September 14, 1984.

Major provisions of this agreement included:<sup>63</sup>

### *Income and Job Protection*

- guaranteed income of 50% of base pay, plus Cost of Living Allowances (COLA), up to age 62 for employees with at least 15 years' service who exhausted supplemental unemployment benefits
- pilot programs at 4 plants to test lifetime employment

### *Plant Closings*

- a 2-year moratorium on closings resulting from the transfer of internally manufactured products to outside sources

### *COLA-Hourly Base Wage*

- previous COLA adjustments deferred for 18 months
- current (last contract's) wage rate maintained

### *Paid Time Off*

- paid personal holidays and December Sunday holiday eliminated

### *Profit-Sharing*

- beginning Jan. 1, 1983, all GM employees would share in the success of GM's US operations.

## The Fremont Plant

The plant designated for the joint venture stood at 45500 Fremont Boulevard, in Fremont, California, on the southeastern rim of the San Francisco Bay (see Exhibit 14). The 411-acre facility had assembled cars and trucks for about 20 years. At peak production, the plant employed some 5,700 workers. In October, 1981, GM canceled truck operations there, which involved 1,200 permanent layoffs, and moved the truck order to St. Louis. In February, 1982, due to slowing sales of the plant's main car outputs, the Oldsmobile Ciera and Chevrolet Celebrity, the second shift on car production was discontinued. That involved another 1,900 workers. Finally, in March, GM closed the plant, idling the 2,500 remaining workers.<sup>64</sup> Community response seemed muted compared to similar closings elsewhere. Other high-technology, high-paying industries had moved into the area. The local Chamber of Commerce asserted that high-tech growth had already replaced most of the 2500 jobs recently lost.<sup>65</sup> Unemployment in the area, at 8.8%, fell below the national average.

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Laid-off plant workers, however, felt differently. In 1983, most remained unemployed and eager to be represented by their local union, UAW Local 1364, in the negotiations between GM and Toyota. Local members contended that both GM and Toyota had implied that most of the joint venture's 3,000 jobs would go to the laid-off Fremont workers. They were accustomed to belonging to a union with a strong bargaining position. They also were prepared to insist that workers be hired and assigned to well-defined jobs, as they always had been, based on criteria of seniority. Seniority was their most important concern. As one Fremont worker put it, "The cultures are so different over there . . . It's probably close to slavery over there," and "They may be great to work for. But . . . if they don't do things the American way, they won't ship one car out of that plant."<sup>66</sup> Toyota, on the other hand, also had concerns. The plant carried a reputation for absenteeism (20%), grievances (800 pending in March, 1982), drug abuse, and violence.<sup>67</sup> Toyota management worried that it faced an uphill battle installing its systems and achieving its customary productivity levels in Fremont.

The Fremont plant held a legacy of labor distrust of management, which existed well before Toyota's involvement. Despite a distinguished production record -- and winning GM's highest quality rating on truck production -- Fremont lost its production mandate to a plant in St. Louis. Prior to the closing, plant management offered incentives for attendance and productivity on the truck assembly line, with an implied promise that the production would remain in Fremont. Since the switch to St. Louis, members of the permanently furloughed work force had retained a strong sense of betrayal.<sup>68</sup>

The International UAW, under Owen Beiber's new leadership, had a slightly different perspective. It did not wish to risk the loss of 3,000 union jobs to a non-union shop over the local's claims. As the consultant to the joint venture, William J. Usery, pointed out, "I certainly recognize the concerns of laid-off workers at Fremont. But no one else is going to use that plant."<sup>69</sup>

Compounding the situation, a nearby Ford plant closed shortly before the negotiations, idling 2,000 more automotive workers. (Thus, since October, 1981, over 7,700 auto workers had been laid off in the area.) While GM typically paid upwards of \$13 per hour, most of the unskilled workers could not expect to earn more than \$6 per hour at other area jobs. Publicly, Toyota would not concede a role for either the international or local UAW in the joint venture.

## **IX. WILLIAM J. USERY**

Acting on the matter of the labor relations structure, intermediaries for Toyota contacted William Usery, a former US Secretary of Labor. Toyota's first discussions with Usery struck him as very vague: He was not told the prospective client's name or specific concern. On March 3, however, Toyota retained him by verbal contract as a consultant to the joint venture responsible for working out an agreement with the UAW.<sup>70</sup>

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Usery had a distinguished career in labor relations. Starting out as a machinist in 1942, he became a representative for the International Association of Machinists in 1956. He went on to serve as US Secretary of Labor in 1976 and 1977, after which he formed and became president of his own consulting firm, Bill Usery Associates in Washington, D.C.

Usery demonstrated sensitivity to the nature of his role from the very beginning. While Toyota wanted him to work solely for the Japanese company, he suggested that he serve as "facilitator." He intended to foster credibility for the JV and cooperation from the UAW.

During March, 1983, Usery met with Toyota's general counsel, Takeo Tsukada, Managing Director Iwasaki, and other top officials in California. Later he met with Tatsuro Toyoda, a managing director informally announced as JV president and CEO on March 21. Usery also met with UAW President Douglas Fraser and the GM Department director, Owen Beiber. Usery found Fraser extremely supportive. Beiber seemed less committed.

In April, Usery went to Japan to meet with top Toyota executives. Eiji Toyoda formally endorsed his role as consultant. GM and Toyota also agreed at this time that Toyota would assume sole responsibility for working out a labor agreement for the joint venture. Not long after his return, on May 12, 1983, Usery held a press conference in which he announced his role and the willingness of Toyota to use former GM employees as the "primary source" for recruitment.

## **X. ANTITRUST REGULATIONS IN THE US**

The remaining party to the undertaking was the US Federal Trade Commission (FTC), which had yet to rule on whether the joint venture violated antitrust regulations. At the time of the negotiations, outsiders believed that two of the five voting commissioners favored the Toyota-GM arrangement and two disfavored it. The tie-breaking opinion belonged to a member whose tenure on the commission would draw to a close within the year. But rumors suggested that the chairman, James C. Miller, a Ronald Reagan administration appointee, would abstain from the decision to avoid an appearance of conflict-of-interest stemming from previous consulting work with GM.

### **FTC Mandate and Organization**

The US Congress legislated the Federal Trade Commission into existence in 1914, and gave it joint responsibility with the Justice Department for enforcing antitrust laws. As described in the *Congressional Quarterly*, The Federal Trade Commission Act "sought to make the new agency the federal government's chief trust-buster. The wording of the legislation was intentionally flexible; Section Five of the act gave the FTC broad powers to define business practices that constituted 'unfair methods of competition'."<sup>71</sup> Congress also passed the Clayton

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Act (frequently referred to as the Clayton Antitrust Act) in 1914. The Clayton Act prohibited specific business activities that "tended to lessen competition or to create monopolies."<sup>72</sup>

Possible antitrust violations generally came to the attention of the FTC through media reports or complaints of citizens or competitors. The commission enjoyed broad investigative powers to access documentary evidence, require the submission of annual and special reports, and issue subpoenas. Proceedings against alleged violations took place on either a formal or informal basis. Formal proceedings took the form of a hearing before an FTC administrative law judge. Decisions became final after 30 days, unless appealed to the full commission. Companies had recourse to district courts. The commission also relied on the district court to enforce its rulings, if necessary, assessing fines of up to \$10,000 per day.

Informal proceedings entailed a variety of outcomes and instruments. The FTC issued advisory opinions and trade regulations. Sometimes letters of discontinuance or affidavits from alleged violators were accepted, if they provided credible evidence that they had complied with FTC guidelines and would not resume the sanctioned practices.<sup>73</sup>

The FTC consisted of five voting members, supported by an administrative and enforcement bureaucracy (see Exhibit 15).

### Considering the Joint Venture Proposal

The proposed GM/Toyota joint venture prospectively involved the world's first and third largest automakers in activities in the world's largest market. As such, the issue had both political and economic ramifications. Ford, Chrysler and even Nissan lobbied hard to draw attention to the JV's likely effects on competition. But the government had also to consider that approximately 12,000 direct and indirect jobs were expected through the venture.

Critics responded that 19,500 jobs would be lost if the venture were allowed, since the new vehicles would probably replace the Chevette. Most of the components and other inputs to the new model would, they charged, originate in Japan, including parts and production equipment, engineering and design. Others argued that Toyota's investment represented a smaller contribution to the American economy than the \$300 million Honda was spending on its plant in Ohio, and the \$600 million Nissan was putting into a light truck plant in Tennessee.

In some observers' views, Toyota would enjoy a virtual free ride around the protectionist politics going on in Congress and around Japan's voluntary export restraints. Toyota would gain access to GM's market and labor relations expertise for a far smaller investment than necessary to build a plant from scratch. Ford further asserted that the joint venture would free GM to divert more resources to large car production, a market segment in which it already held a significant lead.<sup>74</sup>

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## Commissioners' Apparent Positions

On the political side, James C. Miller, Chairman of the Federal Trade Commission, was believed to favor President Ronald Reagan's philosophical goal of reducing regulatory burdens on US business. Miller had replaced former chairman Michael Pertschuk as chairman in September, 1981. Pertschuk, a Jimmy Carter appointee, remained on the commission as a regular member. He remained influential, especially with the aid of his frequent ally, David Clanton. Clanton's term, however, was to expire in four months, on September 25, 1983.

## XI. THE DEADLINES APPROACH

GM and Toyota agreed to commit best efforts to complete this last set of agreements by May 15. On May 25, the first formal, Toyota-UAW negotiations were held, with only 3 weeks remaining of the 120-day period. Friday, June 17 was the last day of the 120-day period agreed in the MoU. If no agreement could be reached by then and one party notified the other that it would not proceed because of an unfavorable labor structure or governmental review, GM was to bear all costs of activities associated with the JV to date.

How would Roger Smith, Eiji Toyoda, their negotiators, Bill Uery, the UAW representatives, and the FTC commissioners and staff proceed?

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